

SETTLEMENT AGREEMENT

This Settlement Agreement ("Agreement") is entered into between the United States of America, Department of Energy, acting by and through the Bonneville Power Administration ("BPA"), and Puget Sound Energy, Inc. ("Puget"). BPA and Puget shall be referred to collectively as "the Parties."

WHEREAS, on May 14, 2001, BPA announced that the transfer capability of a constrained portion of its transmission system known as the West of Hatwai cutplane would be reduced, thereby resulting in curtailments of transmission service across the cutplane unless the Colstrip owners were to install generation dropping equipment on the Colstrip Plant;

WHEREAS, Puget and BPA are parties to an Integration of Resources Agreement, BPA Contract No. DE-MS79-94BP93947, as amended (the "IR Agreement"), which requires BPA to make power available to Puget at various points of delivery on a firm transmission basis;

WHEREAS, Puget alleges that BPA breached its obligations under the IR Agreement by curtailing Puget's east-to-west transmission on a firm basis across the West of Hatwai cutplane on several occasions in the Spring and Summer of 2001;

WHEREAS, on August 10, 2001, Puget filed a Petition for Review Under the Northwest Power Act, Declaratory Judgment and Money Damages in the United States Court of Appeals for the Ninth Circuit, Docket No. 01-71348 (the "Petition for Review"), seeking judicial review of BPA's decision to curtail firm transmission across the West of Hatwai cutplane;

WHEREAS, BPA alleges that under certain provisions of the IR agreement it is entitled to curtail firm transmission across the West of Hatwai cutplane;

WHEREAS, BPA denies that it curtailed Puget's firm transmission across the West of Hatwai cutplane at any time; and

WHEREAS, the conditions giving rise to the curtailments on the West of Hatwai cutplane still exist and will continue to exist for some time.

NOW, THEREFORE, the Parties agree as follows:

1. Definitions. For purposes of this Agreement, the following terms shall have the following meanings:

1.1 All Lines in Service: This condition exists when all of the facilities identified in Attachment A to this Agreement are in service. An "All Lines in Service" condition does not exist during an Emergency Outage, an Urgent Outage or a Routine Outage.

1.2 Emergency Outage: An unanticipated outage of one or more of the facilities identified in Attachment A that occurs unintentionally or that BPA must take immediately in order to repair damaged or malfunctioning equipment that jeopardizes the reliability or safety of BPA's transmission system. An emergency outage shall be considered unintentional if it is caused by the intentional act of a third party who is not subject to BPA's influence, direction or control. BPA is not required to provide advance notice of an Emergency Outage to Puget.

1.3 Urgent Outage: An unanticipated outage of one or more of the facilities identified in Attachment A that BPA must take soon in order to repair damaged or malfunctioning equipment that has a potential for jeopardizing the reliability or safety of BPA's transmission system. In order for an outage to constitute an Urgent Outage, BPA must provide Puget with at least twenty-four (24) hours advance written notice of the outage.

1.4 Routine Outage: An outage of one or more of the facilities identified in Attachment A that is for purposes of performing maintenance, repair or system improvements on BPA's transmission system that are necessary to preserve or improve the reliability or safety of BPA's transmission system. In order for an outage to constitute a Routine Outage, BPA must provide Puget with at least one hundred and sixty eight hours (1 week) advance written notice of the outage.

1.5 Effective Date: The date on which this Agreement has been executed by both Parties.

2. Written Notice: The means of providing the written notice required by sections 1.3 and 1.4 may include, but shall not be limited to, electronic mail (e-mail); provided that, if BPA's e-mail system is inoperable or not functioning BPA must provide notice by some other means.

2.1 The written notice required by this section shall be provided to the following person:

For Puget:

(1) email: BPA-Notices@Puget.com

(2) Doug Faulkner
Puget Sound Energy, Inc.
One Bellevue Center
411 – 108th Avenue
Bellevue, WA 98004

email: dfaulk@Puget.com
Tel: 425/462-3352
Fax: 425/462-3465

(3) Joe Seabrook (GEN-04W)
Puget Sound Energy, Inc.
P.O. Box 90868
Bellevue, WA 98004

email: jseabr@Puget.com
Tel: 425/462-3577
Fax: 425/462-3344

2.2 Puget may change the information provided in Section 2.1. Any change shall be effective five (5) days after Puget provides the new information to BPA.

3. Payment for Curtailments. BPA will pay Puget 50 percent of costs resulting from curtailments of PUGET's transmission service on the West of Hatwai cutplane with All Lines In Service pursuant to the formula set forth in Attachment B.

3.1 Puget will submit an invoice and documentation of any costs that Puget incurs under this Section 3 to BPA. If BPA determines that the documentation is sufficient to establish Puget's costs, BPA shall pay Puget within 30 days of the date of the invoice. Upon request of BPA, Puget shall provide BPA with any additional information reasonably necessary for BPA to verify Puget's costs. BPA shall pay Puget within 14 days of receipt of all additional information necessary to establish Puget's costs.

3.2 Notwithstanding Section 3.1, if BPA disputes Puget's documentation or determines that the documentation is insufficient to establish Puget's costs, BPA shall pay Puget any undisputed amounts and shall provide Puget with a written explanation as to why Puget's documentation is insufficient to establish

the disputed costs. If it should later be determined in arbitration pursuant to Section 11 of this Agreement that Puget's documentation was sufficient to establish its costs, then BPA shall pay Puget interest on the amount found due Puget, accruing from fourteen days after the date that BPA received sufficient documentation. The interest rate shall be the interest rate then established pursuant to 41 USC § 611. Arbitration of issues under this Section 3 may include other issues related to the curtailment or this Settlement Agreement that the parties wish to raise.

4. Verification of Outage. Upon request of Puget, BPA shall promptly provide Puget with written documentation or other substantiation reasonably sufficient to establish whether an All Lines In Service condition did or did not exist for any curtailments of Puget's transmission service on the West of Hatwai cutplane.

5. West of Hatwai Scheduling Procedure. BPA will adhere to the West of Hatwai Scheduling Procedure posted on its Open Access Same-Time Information System ("OASIS"), a copy of which is Attachment C to this Agreement. BPA may unilaterally amend such Scheduling Procedure, except that BPA may not make any amendment to such Scheduling Procedure if the effect of the amendment is to reduce the amount of power that Puget can schedule under the IR Agreement.

6. Limitation on New Arrangements for Firm Transmission Service. BPA will not enter into any new arrangements to provide any firm transmission service east-to-west across the West of Hatwai cutplane after the Effective Date until there is a WECC-approved OTC limit for east-to-west transmission across the West of Hatwai transmission path under which BPA's share of such OTC exceeds 2200 MW during all seasons without a remedial action scheme ("RAS") for direct tripping of the Colstrip Plant. However, BPA may enter into new arrangements to provide firm transmission service east-to-west across the West of Hatwai cutplane after the Effective Date if BPA's share of such WECC-approved OTC limit exceeds 2200 MW during all seasons with a RAS for direct tripping of the Colstrip Plant provided that Colstrip owners with the authority to do so (which must include, however, both PUGET and Portland General Electric Company ("PGE")) have executed a written agreement with BPA to provide such direct tripping. In all cases BPA shall be limited to entering into new arrangements to provide firm transmission service east-to-west across the West of Hatwai cutplane to the amount by which BPA's share of the OTC of the West of Hatwai transmission path in an east-to-west direction exceeds 2200 MW.

7. Dismissal of Complaint. Within 30 days of the Effective Date, Puget will dismiss with prejudice the Petition for Review and will not bring any legal action against BPA, either during the term of this Agreement or after its termination, for

curtailments on the West of Hatwai cutplane that take place during the term of this Agreement.

8. Term and Termination. This Agreement will terminate when there is a WECC-approved OTC limit for east-to-west transmission across the West of Hatwai transmission path under which BPA's share of such OTC exceeds 2200 MW during all seasons either (1) without a RAS for direct tripping of the Colstrip Plant; or (2) with a RAS for direct tripping of the Colstrip Plant, provided that Colstrip owners with the authority to do so (which must include, however, both Puget and PGE) have executed a written agreement with BPA to provide a RAS for direct tripping of the Colstrip Plant. Puget may terminate this Agreement earlier if it has incurred at least \$2 million of costs as its share of replacement power and transmission costs under Section 3 of this Agreement. Puget also may terminate this Agreement if a Routine Outage exceeds thirty (30) days.

9. Future Legal Actions. The Parties agree that Puget shall be entitled to bring legal action(s) for any curtailments that take place after the termination of this Agreement. In the case of a curtailment that begins before the termination of this Agreement and continues after termination, Puget shall be entitled to bring a legal action only for the portion of the curtailment that takes place after the termination of this Agreement. BPA will not assert in any such legal action, nor encourage either directly or indirectly any other entity to assert, that the statute of limitations or the time for filing such legal action began to run at any point before the termination of this Agreement.

10. Effect of Agreement. This Agreement does not constitute an admission by either party regarding the parties' respective rights under the IR Agreement and shall not serve as an interpretation of such Agreement or as precedent for any future action or dispute. This Agreement will not be admissible regarding the parties' respective rights under the IR Agreement or for any other purpose in any future court proceeding or administrative proceeding, except that this Agreement is admissible to effectuate the terms of this Agreement or in any action alleging a breach of this Agreement.

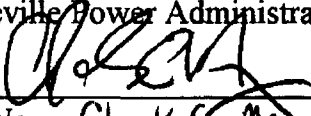
11. Arbitration. All disputes arising under or related to this Agreement will be resolved through binding arbitration pursuant to the Commercial Arbitration Rules of the American Arbitration Association. Judgment upon the award rendered by the arbitrator(s) may be entered in any court having jurisdiction thereof.

12. Counterparts. This Agreement may be executed in counterparts by the Parties and such counterparts, once executed, shall together constitute one final

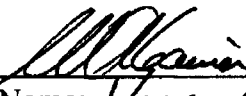
agreement binding the Parties to this Agreement as if one document had been signed by both Parties.

IN WITNESS WHEREOF, intending to be legally bound, the Parties hereto have fully executed this Agreement in counterparts effective as of the Effective Date.

UNITED STATES OF AMERICA
Department of Energy
Bonneville Power Administration

By: 
Print Name: Chuck E. Mejer
Title: Vice President Marketing & Sales
Date: 7/9/02

PUGET SOUND ENERGY, INC.

By: 
Print Name: William A. Gaines
Title: Vice President, Energy Supply
Date: 6/24/02

ATTACHMENT A

1. DWORSHAK -TAFT 1 (500 kV)
2. G COULEE-BELL #3 (230 kV)
3. G COULEE-BELL #5 (230 kV)
4. G COULEE-WESTSIDE 1 (230 kV)
5. HATWAI-DWORSHAK 1 (500 kV)
6. WESTSIDE-BELL (230kV)
7. HATWAI-LOWER GRANITE (500 kV)

ATTACHMENT B

BPA Payment = 50%[(Market Value at Mid-C) - (Cost of Colstrip) - (Profit from Alternate Sales)]

Market Value at Mid-C = (MW Curtailed on-peak)(Hours of Curtailment on-peak)(Appropriate Mid-C Index for on-peak hours) + (MW Curtailed off-peak)(Hours of Curtailment off-peak)(Appropriate Mid-C Index for off-peak hours)

Cost of Colstrip = (MW Curtailed WOH)(Hours Curtailed)(Incremental Cost)

Profit from Alternate Sales = (MW sold)(Hours)[Alternate sale price - (Incremental Cost + Trans)]

Appropriate Mid-C Index = (a) for day-ahead curtailments, the Dow Jones Mid-C Firm Power Index or if the Dow Jones Mid-C Firm Power Index is not available another applicable index that provides similar information; and (b) for real-time curtailments, the Powerdex Mid-C Index, if available; and if it is not available, a comparable hourly index; and if no comparable hourly index is available the daily Dow Jones Mid-C Firm Power Index. The parties can mutually agree to use an hourly index other than the Powerdex Mid-C index if and when another hourly index becomes available.

Example #1

Mid-Columbia Index = \$30/MW hr

WOH curtailment = 100 MW's

Length of Curtailment = 10 hours

Colstrip Output reduced by 100 MW's

Incremental Cost of Colstrip = \$10 (assumed for example purposes only)

BPA Payment = 50%[(Market Value) - (Cost of Colstrip) - (Profit from Alternate Sales)]

= 50%[(100MW)(10hr)(\$30/MWh) - (100MW)(10hr)(\$10/MWhr)]

$$= 50\%[\$30,000 - \$10,000 - \$0]$$

$$= \$10,000$$

Example #2

Mid-Columbia Index = \$30/MWhr

WOH curtailment = 100 MW's

Length of Curtailment = 10 hours

Incremental Cost of Colstrip = \$10 (assumed for example purposes only)

Alternate sale = 50 MW

Price of Alternate sale = \$27/MWhr

Alternate transmission = \$7/MWh

Alternate sale for 10 hours

Payment = 50%[(Market Value) - (Cost of Colstrip) - (Profit from Alternate Sales)]

$$= 50\%[(100\text{MW})(10\text{hr})(\$30/\text{MWh}) - (100\text{MW})(10\text{hr})(\$10/\text{MWh}) - (50\text{MW})(10\text{hr})[\$27/\text{MWh}$$

$$- (\$10/\text{MWh} + \$7/\text{MWhr})]$$

$$= 50\%[\$30,000 - \$10,000 - \$5,000]$$

$$= \$7,500$$

ATTACHMENT C

WEST OF HATWAI SCHEDULING PROCEDURE Sixth Update on West of Hatwai Scheduling Procedure

Posted June 29, 2001

Revised: July 10, 2001, July 23, 2001, August 3, 2001, August 9, 2001,
April 3, 2002, and April 15, 2002

The purpose of this posting is to make two clarifications regarding the West of Hatwai scheduling Procedure. The first item pertains to schedules that move over Avista Transmission's share of West of Hatwai and which are then delivered to BPAT on the west side of the cutplane. These schedules are delivered to BPAT at the Mid-Columbia at Vantage Substation since this is where Avista and BPAT interconnect west of the West of Hatwai cutplane. Due to the need for accurate information for tracking and tagging purposes, customers who deliver to BPAT over Avista's West of Hatwai transmission capacity must specify "MIDCRemote" as the point of interconnection between Avista and BPAT on the tag. Please refer to BPAT's Remote Resource Business Practice posted July 3, 2001. In addition, the actual schedule must use the designation "AV*M" as the source in the scheduling account title, not "AVA".

Furthermore, OASIS reservations must also specify "MIDCRemote" as the point of interconnection between Avista and BPAT if the customer is using Avista's share of the cutplane to get across West of Hatwai. Westbound reservation requests that specify "AVA.BPAT" as the point of receipt use BPAT's share of the West of Hatwai cutplane. "AVA.BPAT" is acceptable as a point of interconnection to deliver to Avista, Columbia Falls Aluminum, Kaiser Bell, Kaiser Trentwood, Pend Oreille, Inland Power & Light, Northern Lights, Lincoln Electric Coop, Kootenai Electric Coop, City of Troy, Montana, and the City of Bonners Ferry. These points of receipt/points of delivery combinations do not cross the West of Hatwai cutplane.

The second clarification regards the availability of short-term firm and hourly firm transmission. BPAT has not made firm transmission available over its share of West of Hatwai nor will any be made available until further notice.

Posted April 15, 2002

Fifth Update on Proposed New West of Hatwai Scheduling Procedure

The purpose of this posting is to make two clarifications regarding the West of Hatwai scheduling Procedure. The first item pertains to schedules that move over Avista Transmission's share of West of Hatwai and which are then delivered to BPAT on the west side of the cutplane. These schedules are delivered to BPAT at the Mid-Columbia at Vantage Substation since this is where Avista and BPAT interconnect west of the West of Hatwai cutplane. Due to the need for accurate information for tracking and tagging purposes, customers who deliver to BPAT over Avista's West of Hatwai transmission capacity must specify "MIDCRemote" as the point of interconnection between Avista and BPAT on the tag. Please refer to BPAT's Remote Resource Business Practice posted July 3, 2001. In addition, the actual schedule must use the designation "AV*M" as the source in the scheduling account title, not "AVA".

The second clarification regards the availability of hourly firm. BPAT has not made hourly firm available over its share of West of Hatwai nor will any be made available until further notice.

Posted April 3, 2002

Fourth Update on Proposed New West of Hatwai Scheduling Procedure

The purpose of this posting is to make one correction to the description of the new scheduling procedure. The earlier versions of the description read, "BPAT would continue to deny non-firm preschedules over WOH when a curtailment situation exists." This should have read, "BPAT will continue to deny non-firm east to west preschedules over WOH until further notice.

There are no restrictions on west to east schedules over WOH." The description below has been modified to reflect this correction. BPAT will continue to allow non-firm schedules on real-time if there is ATC available.

Posted August 9, 2001

The software development required for BPAT to implement the proposed new West of Hatwai (WOH) scheduling procedure will be completed on Wednesday, August 8, 2001. The new procedure will take effect on Friday, August 10, 2001 (preschedule on Thursday, August 9, 2001). The procedure will be as described below. BPAT has made one addition to the procedure. If the Operational Transfer Capability (OTC) of WOH is forecast to be below 1800MW on either preschedule or for a future hour(s) during the current operating day, then BPAT will revert back to our standard practice of providing the firm contract holders with pro rata allocations for the preschedule or future hour(s) and limiting firm schedules so that these allocations are not exceeded.

BPAT feels that this addition to the procedure is prudent because of the high likelihood that schedules would otherwise have to be curtailed in real-time if the OTC dropped below 1800MW due to the relatively high usage of WOH. Under current nomograms, the OTC of WOH does not drop below 2050MW if all facilities are in service. Hence, an OTC below 1800MW and the resulting change in procedure should only occur for significant outages.

DESCRIPTION OF NEW SCHEDULING PROCEDURE:

The basic principles of the new scheduling procedure for WOH would be that firm customers would be allowed to schedule up to their firm contract demand on preschedule. BPAT will continue to deny non-firm east to west preschedules over WOH until further notice. There are no restrictions on west to east schedules over WOH. No firm curtailments would be imposed during the preschedule process. BPAT would readjust net schedules in real-time that exceed BPAT's share of the West of Hatwai Operational Transfer Capability (OTC), as discussed in the paragraph below.

The method to readjust net WOH schedules, if necessary, that are greater than BPAT's share of the WOH OTC in real-time, would be as follows: 1) BPAT would first curtail any non-firm transmission schedules over the WOH path that may have been previously scheduled in real-time; 2) Using the OTC for WOH, BPAT would compute the pro rata allocation of capacity for all BPAT firm contract rights holders based upon total long-term firm rights pursuant to each customer's transmission agreement; 3) BPAT would then determine which customers were scheduling in excess of their calculated pro rata firm allocation; 4) BPAT would then pro rate these firm schedules down (excess schedules) and notify customers of their need to reduce schedules until the overall net WOH schedule was back within BPAT's share of the WOH OTC.

Customers whose schedules were less than or equal to their pro rata allocation would not be curtailed. This procedure would apply for within hour, as well as the next scheduling hour, as required.

If the WOH OTC is forecast at preschedule to be below 1800MW, would revert back to standard scheduling procedures. BPAT would provide firm customers with pro rata allocations prior to preschedule and the firm preschedules could not exceed these pro rata allocations. The same procedure would be followed in the current day if the WOH OTC for a future hour were forecast to be below 1800MW. BPAT would notify firm customers of their pro rata allocations for that future hour and would limit firm schedules to be within the allocations.

Posted August 3, 2001

REVISED Update on West of Hatwai Curtailments

BPAT is completing operating studies of transfer limits for the West of Hatwai path and seeking WSCC approval of the transfer limits. It is anticipated that these new studies will show increased transfer capability over West of Hatwai. In the meantime, the new Rathdrum Generation Project will go on-line and begin exercising its West of Hatwai rights starting July 1, 2001. In addition, NT customers with federal generation in the area are expected to exercise their West of Hatwai rights later in the week of July 1 in order to meet fish mitigation requirements. Furthermore, other changes to some existing contracts may reduce the respective contracts' demand over West of Hatwai. These generation and contract changes will result in changes to the curtailment levels seen by all users of the West of Hatwai path. Firm PTP, IR, and FPT demands will be curtailed on a pro rata basis with the redispatch of NT customer generation over West of Hatwai.

BPAT is also in the process of developing a new scheduling procedure for West of Hatwai to minimize the amount of curtailment to its customers. BPAT hopes to have this new scheduling procedure in place by July 6. BPAT will provide further information during the week of July 1 to customers on the specifics of the new procedure and the timeline for its implementation. Until this new scheduling procedure is in place, BPAT customers who use the West of Hatwai cutplane will be notified of curtailments (both preschedule and real-time) under BPAT's current procedures.

Posted June 29, 2001

WEST OF HATWAI SCHEDULING PROCEDURE

Additional Update on Proposed New West of Hatwai Scheduling Procedure

On June 29, 2001, BPAT posted "Revised Update on West of Hatwai Curtailments" announcing that BPAT anticipated increased transfer capability over the West of Hatwai (WOH) cutplane and was developing scheduling procedures to minimize curtailments to our customers. The June 29th Posting said that BPAT hoped to have the new scheduling procedures in place by July 6, 2001 (Posting is copied below).

This Posting is to inform customers that the required software development for the new scheduling procedures may take an additional 2 weeks for testing and implementation. Therefore, BPAT estimates that the new procedure will go into

effect around July 24. BPAT will continue to update its customers on the implementation progress for this new scheduling procedure.

Posted July 10, 2001

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